fa insight
TD Ameritrade Institutional Benchmarking

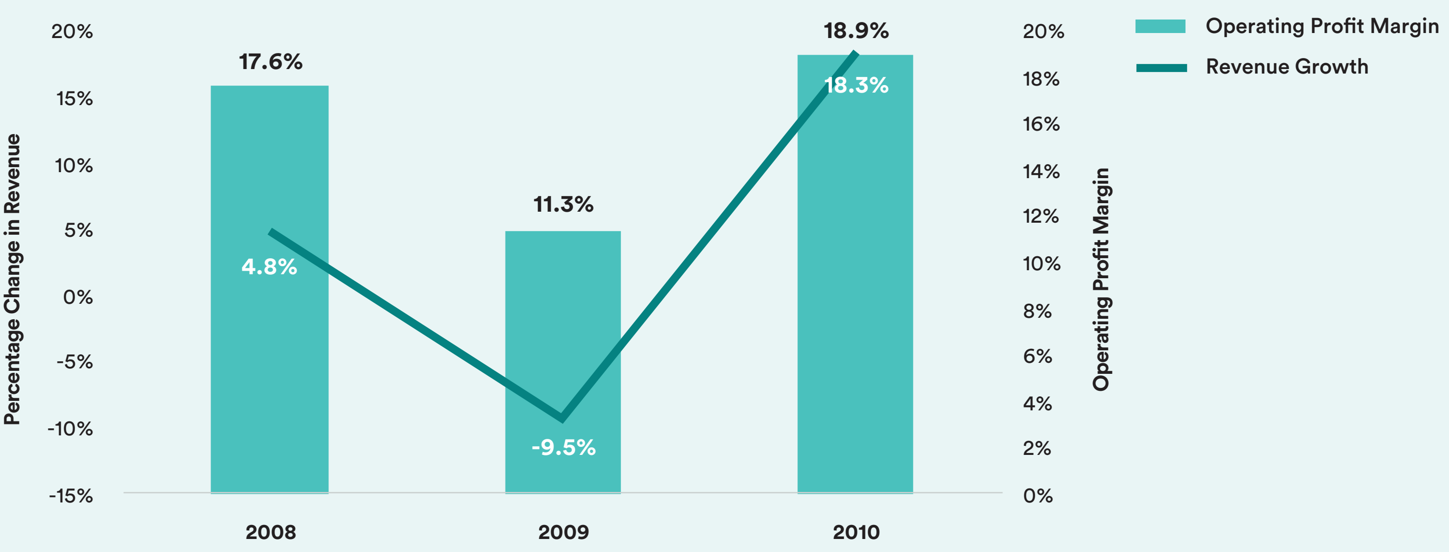
Lessons from the Great Recession

Excerpt from *The 2020 FA Insight Study of Advisory Firms: Growth by Design*

Looking back can often be an invaluable tool for determining the best way forward. Reflecting on the experiences of advisory firms through the Great Recession offers insight into what can be expected in the months and years ahead, as well as what firms should emphasize to better ensure future success. While the conditions that firms face today aren't exactly comparable, enough similarities exist to make this exercise worthwhile. In particular, the behaviors demonstrated by the best-performing firms during the Great Recession provide some pertinent lessons for firms today. These better performers demonstrated the possibility of not just surviving but thriving in turbulent times.

As the recession officially took hold in December of 2007, effects were most apparent the following year in the form of just 4.8% annual revenue growth (Figure 1). Median operating profit margin, at 17.6%, remained healthy. The recession's full impact came in 2009, probably the worst year for advisory firms in the 12 years of annual FA Insight studies. Despite the recession officially concluding mid-year in June, annual revenue dropped nearly 10% for the typical firm. The median profit margin dropped over six percentage points, but even at 11.3%, profitability was likely the envy of many other industries.

Figure 1
Revenue Growth and Profitability, 2008–2010



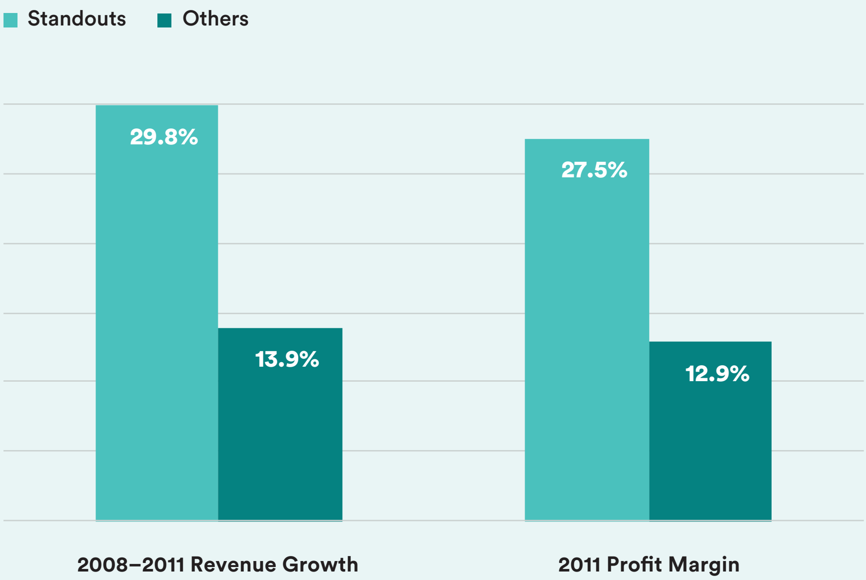
By 2010, recovery was well underway. Profitability bounced back to above its pre-recessionary level. Median revenue growth, nearly 19%, set a record high that still stands today.

How Standout Firms Stood Out (2008–2011)

While the industry eventually rebounded to new levels of success, the Great Recession obviously resulted in some challenging years for advisory firms. For a subset of select firms, however, the period proved far less painful. These firms saw a once-in-a-decade opportunity to more clearly demonstrate their value and turn a crisis into a market advantage. This same type of attitude can also help propel today's firms to move through and beyond the current pandemic.

For a closer look at best business practices during challenging economic times, we tracked the performance characteristics of the same 39 advisory firms that consistently participated in FA Insight studies during and after the Great Recession (Figure 2).

Figure 2
2008–2011 Revenue Growth and 2011 Profitability Define Standouts



Standouts more than doubled others in terms of:

- Three-year revenue growth
- 2011 operating profit

The firms in this group with above-average revenue growth during the 2008-2011 period and an above-average operating profit margin in 2011—a third of the group—were considered "Standouts." (Note: This is a slightly modified Standout methodology than what is usually applied in our annual studies.)

Perhaps more so than in a less volatile period, a wide gap existed when benchmarking the performance of these Standout firms versus others. The differences can be distilled to a few key practices:

Sustained business development. When markets are volatile, clients are often the most reliable indicator of business growth. From 2006 to 2010, Standouts expanded their client bases at an average annual rate of about 10% while other firms added clients at less than 1%. Even in 2009, at the height of the recession, Standout client growth was 5% while growth for other firms was nearly flat.

Standout firms consistently attracted new clients to their firms before and after the recession. They never wavered from their focus on growth.

10%
Standouts
Average annual client growth rate, 2006–2010

<1%
All Others
Average annual client growth rate, 2006–2010

While it is understandable for firms to downplay business development during such times of crisis, what is typically overlooked are the opportunities that emerge in tough times. There is no better environment for advisors to demonstrate their value. Further, money is often in motion as investors call into question whether they have access to the right kind of guidance needed for weathering current market volatility.

Team expansion. Standout firms grew in headcount from a median of seven team members in 2007 to ten by 2010, whereas headcount at other firms contracted slightly. It takes a certain amount of courage to hire amid a severe downturn, but there are clear advantages in doing so. First, there is no better time to hire. Talent is in transition as a weakened economy broadens the available labor pool and provides firms with a unique opportunity to engage candidates who may not otherwise be available. But most important, while a firm's revenue outlook may be uncertain, demands on an advisor's time only increase in periods of turmoil. Additional capacity allows enough time for business development and better positions a firm to take advantage of an economic recovery.

Standouts Expand Their Teams

2007   2010

43%
Increase in FTEs
Standouts vs. Others
(2007–2010)

Rising productivity. By 2011, revenue per revenue generator at Standout firms was 22% greater than in 2008, whereas productivity at other firms fell by 10%. Productivity declined sharply for both groups of firms in 2009. For Standouts, this was due to adding capacity at a rate faster than they were increasing revenue. Productivity quickly rebounded, however, and these firms became better positioned for growth in the recovery years that followed. In contrast, productivity continued to decline for other firms, where revenue dropped more sharply due to contracting AUM and lack of capacity for generating client growth.

Managing expenses. Through the recession and into recovery, Standouts managed costs in a way that maintained profitability without slowing growth. For Standouts, the median overhead expense margin dropped from 45% to 31% during the 2008–2011 period. In contrast, the typical overhead margin for other firms first jumped sharply from 46% in 2008 to 56% in 2009 before dropping to a level just below 46% in the years that followed. Standout owners were also quick to adjust their own pay, reducing their compensation as a share of total firm revenue from 31% down to 19%, whereas owner pay at other firms hovered around 25% of total revenue throughout the 2008–2011 period.

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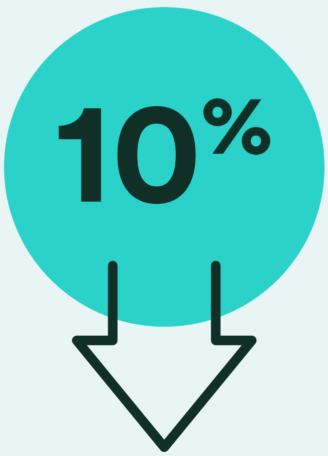
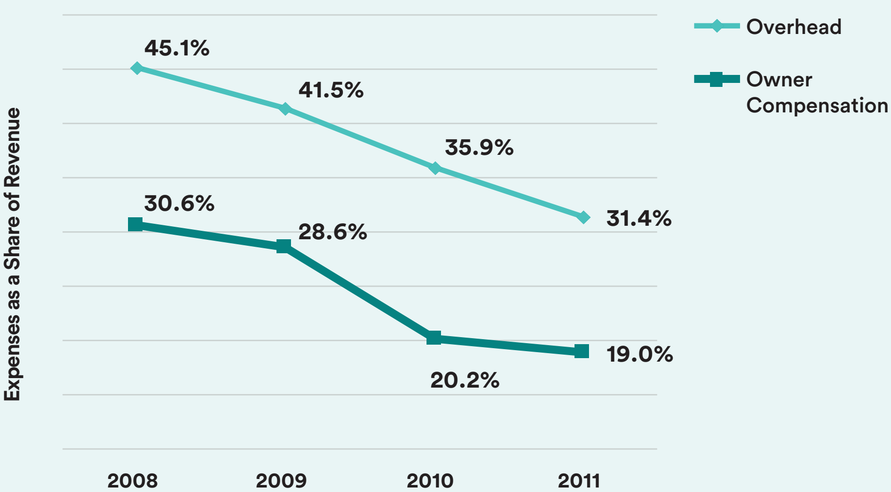


By 2011, productivity at other firms **fell by 10%.**

Figure 3

Standout Expense Margins, 2008–2011



Lessons Learned

Whether it is remaining proactive in terms of business development, continuing to invest in people or selectively pulling back on expenses, across these practices a common theme emerges: These Standout firms resisted the temptation to simply hunker down and wait until the storm blew over. By staying focused on long-term objectives and taking decisive action where needed, these firms gained an advantage in a turbulent time and, as a result, enhanced their chances for even greater success when the economic recovery took hold.

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